

Response to FCA CP25/11

About the Building Societies Association

The Building Societies Association (BSA) represents all 42 UK building societies, including both mutual-owned banks, as well as 7 of the largest credit unions. Building societies have total assets of almost £525 billion and, together with their subsidiaries, hold residential mortgages of over £395 billion, 24% of the total outstanding in the UK. They also hold £399 billion of retail deposits, accounting for 19% of all such deposits in the UK. Building societies account for 40% of all cash ISA balances. With all their headquarters outside London, building societies employ around 52,300 full and part-time staff. In addition to digital services, they operate through approximately 1,300 branches, holding a 30% share of branches across the UK.

Executive summary

We welcome the opportunity to comment on the Mortgage Rule Review and are generally supportive of the proposals. The aim to speed up the process and make it easier for customers to change their mortgage is to be welcomed.

It is 11 years since the implementation of the Mortgage Market Review and as a first step in reviewing regulation to ensure that it remains appropriate and supports innovation, it is a welcome start. There are other areas, specifically to support first-time buyers that could make a material impact, and we look forward to engaging in the discussion paper over the summer on these broader topics.

Although the changes proposed are permissive, our recommendation would be to not implement any changes until the closure of the forthcoming discussion paper and analysis of the responses. There is a risk of unintended consequences with incremental changes in isolation.

As these proposals are permissive changes, it is important that FCA makes this clear in its final policy statement. Clarity that any changes are subject to lenders' risk appetites and commercial decisions are vital. Managing the expectations of prospective borrowers and the Financial Ombudsman Service (FOS) will help to avoid unintended outcomes.

Proposal 1: Mortgage Advice

We can see the benefit of giving customers choice about whether to opt for a fully advised process or utilise an execution only route if that is their preference, irrespective of which channel they engage. With the proposed changes being permissive, firms will make their own commercial decision whether they wish to adopt them.

For some borrowers that know what they want, are financially savvy, and have experience of taking out mortgages in the past, this provides them with another option.

Allowing customers that apply online the opportunity to access personalised costings and ask any questions could enhance the customer experience and also give firms an opportunity to identify if the borrower is at risk of a poor outcome.

There are some considerations to ensure this approach is well executed and delivers the intended policy outcome:

- The CP identifies that 97% of all new mortgage sales are advised. If these changes are implemented, that proportion is likely to fall over time if firms decide to utilise the permissive rule changes proposed. We believe that most consumers will continue to engage the services of a mortgage broker and that the impact on advised sales will likely be in the lender direct channel.
- It is vital that the FCA policy intention is aligned with the Financial Ombudsman Service (FOS) expectations to avoid unintended consequences for firms.
- Firms will need to implement adequate oversight and controls to ensure that the customer is clear that they are not receiving regulated advice. This new flexibility does present a heightened risk of helpful colleagues inadvertently swaying into advice.
- Training and education are vitally important. Additional training may be required for colleagues to identify when a customer could benefit from advice. What does FCA deem to be a suitable qualification for dealing with execution-only enquires? Is the expectation that they are CeMAP qualified?
- Some firms will require investment in digital journeys to support an execution-only process. Therefore, if firms choose to adopt this approach it may take some time to implement this change.

Proposal 2: Remortgage Process

We understand the context and why the FCA is proposing this change, and we welcome attempts to speed up and simplify the mortgage process.

Remortgaging can be challenging and time consuming, however the main challenges with remortgaging do not sit with the lender, but with the conveyancing process. The pain point can be the costs to switch for some, if it is a leasehold flat or there is going to be a change of name for example, these switches have additional costs. The interaction with the lender or broker is relatively straightforward. While the process does require a customer to submit personal information to carry out an affordability assessment and to provide documents to verify income and expenditure, it is straightforward and expected by customers.

The opportunity to use the modified affordability assessment approach to speed up the remortgaging process and enable firms to compare quickly would be a significant change to current practice. Our sense is that currently, few firms plan to adopt modified affordability more widely for remortgages.

Although the change is permissive, and we welcome any opportunity to improve the remortgaging process, we have several considerations in this proposal:

- How will this work practice? What evidence would a lender be expected to see to ensure that the new mortgage is more affordable than offered by the current lender? Could this lead to an increase in false documentation/mortgage fraud? Would it speed up the process?

- There are concerns that when a customer engages with a new firm that is using a MAA, the firm may not know when the customer last had a full affordability check or whether their circumstances have since changed. This leaves a question mark around affordability and knowing if the customer is at risk of experiencing financial difficulty.
- Firms will also need to determine how to evidence that they are meeting the Consumer Duty principles using this approach.
- There is potential for the larger banks to achieve a competitive advantage over the building society sector due to the amount of financial information they can access such as current account activity.
- There is potentially a concern amongst firms that we could see customers chasing the MAA offer with those firms that offer it, rather than the right product for them. There is a concern on how this would be viewed by FOS.

Proposal 3: Term Reduction

Giving customers the flexibility and opportunity to reduce their term simply and without fuss gives customers more autonomy and control over their mortgage payments.

Clearly, since the implementation of the Mortgage Market Review, we have seen mortgage terms lengthening. Most first-time buyers now take terms in excess of 30 years. These terms are not taken lightly and are usually out of necessity to maintain affordable monthly repayments.

The overpayment facility on a mortgage is an alternative and flexible way to reduce the balance and the overall mortgage term.

There are some considerations on this proposal:

- Similar to the above on easier remortgaging, firms will need to determine how they evidence adherence with the Consumer Duty principles when not completing a full affordability check. Will customers understand the full implications of reducing their term?
- Whilst there are currently no major barriers for customers wanting to reduce their mortgage term with a lender, the affordability requirement does add friction to online/digital processes. Increasingly borrowers are choosing to service their mortgage online and this proposal would provide more with the ability to do so.
- Firms will likely put in place a backstop to enable borrowers to return to their original term if they find the new payment difficult to maintain. It would be helpful for FCA to confirm that lenders are able to allow a customer to revert to their original term, but not beyond if needed.

Proposal 4: Removal of guidance

We are supportive of the removal of FG13/7 guidance within the Handbook.

Questions

Question 1: Do you agree with our proposed changes to MCOB to remove the interaction trigger?

We are supportive of the flexibility that this change provides to firms. Enabling consumers to engage in informative interaction and ask questions without triggering the advice requirement could enable more informed decisions about whether they choose a fully advised route or not.

Given these proposed changes are permissive, firms will make their own commercial decisions about whether to provide an execution-only process.

Firms will need to determine how the customer journey would work in practice and undertake training for colleagues. This will ensure that guardrails and clear processes are in place to prevent a customer inadvertently believing that they had received advice.

It is vital that FCA continues to engage with the FOS to mitigate the risk that its interpretation of advice, interactive dialogue and execution-only differs from FCA or firms' processes. This could create an additional risk between firms and FOS.

Question 2: Do you agree with our proposals to amend the circumstances where firms would be required to ensure consumers have made a positive election to use an execution-only channel?

The proposals to change the circumstances where firms would be required to ensure customers have made a positive election to use an execution-only channel suggest that this requirement would be removed in circumstances where there is spoken dialogue (see Section 3.19). However, the proposed rule MCOB 4.8A.14R (5) has only been slightly amended. The intent of this is clearly set out in section 3.19 on the consultation but the drafting of the rule could be clearer.

We would suggest either deleting this rule in its entirety or making it clear that written confirmation from the customer is only required where advice has been rejected. The removal of the requirement to obtain this in writing from customers would be helpful, particularly in the case of digital journeys to avoid unnecessary friction – our current assumption is that any execution-only processes introduced via telephone channels would include some form of questioning of the customer to confirm that they are electing to proceed execution-only but this would likely be verbally.

Question 3: Is there anything else you think we should consider for this proposal (mortgage advice and interactive dialogue)?

No further comments

Question 4: Do you agree that the requirement for a full affordability assessment when reducing the term of a mortgage should be removed [with affordability being assessed in line with a firm's obligations under the Consumer Duty and its responsible lending policy]?

Firms will determine how they will evidence adherence to the requirements set out by Consumer Duty. While we anticipate low demand for stand-alone term reductions this change would benefit the increasing number of customers wishing to manage their mortgage online. It removes the friction of a formal affordability assessment and gives the customer more control.

Question 5: What further regulatory changes could support borrowers to reduce their term when appropriate?

Firms proactively communicate the benefits of shorter terms and the cost implications of longer terms. For example, at natural touch points such as annual statements, rate switches or other contract variations, the firm could encourage customers to consider the impact of the term on the overall cost of their mortgage.

Generally speaking, as most mortgages are currently via an intermediary, a broker will talk in detail to the borrower about taking the mortgage over the shortest affordable term.

We don't believe that further regulation is warranted in this area.

Question 6: To what degree could unaffordable term reductions increase as a result of the proposed approach? Are further mitigants required?

Some borrowers may take a longer term at application to meet affordability criteria and then apply to reduce the term. This could put the borrower at increased risk of financial difficulty in the event of a rate change or when they remortgage or product transfer.

In general, it would be better for the customer to utilise an overpayment facility to reduce the term gradually. This gives them the flexibility to stop overpaying if their circumstances require it.

Firms will develop mitigants to fit with their processes to ensure their customers are not receiving poor outcomes.

Question 7: Is there anything else you think we should consider for this proposal (amending affordability assessments when reducing a mortgage term)?

For many customers, a more flexible approach to shortening their term would be to utilise any overpayment facility rather than a contractual term reduction.

Question 8: Do you agree with developing an alternate, more flexible approach to affordability assessments for remortgaging activity?

This proposal would permit lenders to enter into a new mortgage contract where it is more affordable than a customer's current mortgage, or a new mortgage product from their current lender. However, this presents challenges in how customers would evidence the new mortgage product that is available to them from their existing lender.

Lenders may need to carry out additional checks to mitigate the risk of false documentation or mortgage fraud.

Firms will need to determine how they will evidence adherence to the requirements set out by Consumer Duty if they are unable to evidence sufficient exploration of the customer's affordability and circumstances

This change could potentially give larger firms an unfair advantage over smaller lenders in the market. Large banks may have access to other financial information for the customer such as current account activity reducing the risk of accepting a remortgage application with no affordability assessment. There are therefore

concerns that this proposal could drive undesirable outcomes without firms having access to an open banking model where data is shared.

In addition, larger firms are likely to already have the technology in place to support the implementation of this proposal. Many smaller lenders do not currently have the technology to accept applications based on MAA therefore this change would potentially require the need for significant investment and system changes if it is to make a material difference in the market.

Question 9: Do you agree with our proposal to extend the use of the MAA in this way?

The introduction of the MAA limits the assessment of a borrower's affordability and ongoing creditworthiness, effectively placing reliance on the previous lender's assessment. It also assumes that nothing significant has changed since that assessment that exposes the customer to an increased likelihood of credit impairment or financial difficulty.

Without a thorough assessment, this could expose the customer to an increased risk of arrears.

While the intent is laudable, the operational success of this proposal is heavily dependent on improving data access and digitisation within the remortgage market.

Question 10: What evidence (if any) would the new lender need from the customer or their existing lender to confirm the MAA and new product can be made available to the customer?

Evidence would be required of rates available to the customer in question, or at least retention rates available to all customers, which would then require the FCA to provide clarity on what basis the assessment of 'more affordable' would be based. (i.e. would the new lender compare to the highest available rate)?

Larger firms or banks may benefit disproportionately from this change due to better access to customer data and financial performance insights, such as current account performance. There is a risk that this will unfairly disadvantage smaller firms and building societies.

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Question 11: What barriers may lenders or consumers face in making use of the proposed approach? How might they be overcome?

There are a number of potential barriers to lenders and consumers in making use of the proposed approach.

Significant system development will likely be required to remove or adapt the affordability assessment.

The ability of a lender to obtain, or a customer to provide evidence that the new mortgage will be more affordable.

The ability for lenders to provide what is necessary or requested by other lenders adopting MAA's.

Training and competency requirements for colleagues involved in these transactions.

Monitoring performance of these cases to evidence good outcomes.

A recurring potential barrier with the proposals is also the FOS interpretation and application of these changes. This is front of mind for all lenders with moves towards outcome-based regulation.

Question 12: Is there anything else we should consider for this proposal (amending MAAs when remortgaging)?

One approach to providing suitable evidence would be to rely on customer declaration or information obtained from credit reference agencies as part of standard credit checks. Another option could be to ask the customer to provide their latest annual mortgage statement or assess the retention products from the current lender.

As set out in section 3.49 of the consultation paper, firms could be at risk of future complaints if customers later fall into financial difficulty, and it comes to light that a full affordability assessment at inception would have determined the loan was unaffordable.

Question 13: What further regulatory changes, if any, could support simpler remortgaging?

Existing regulations already support this customer cohort while ensuring responsible lending. Firms can apply differentiated stress tests for product terms of ≤ 5 years versus > 5 years and can stress at pay rate for like-for-like remortgages if firms choose to.

Some firms will consider reducing stress tests under certain circumstances, but this is unlikely to be to the pay rate. A significant challenge is lender system capability, as many can only apply one stress rate across all lending, which would create a competitive advantage for lenders capable of applying differentiated stress tests by cohort.

Question 14: Do you agree with our proposal to retire FG13/7?

Yes.

Question 15: Do you agree with our proposal to retire FG24/2?

Yes we agree with the removal of FG24/2, ongoing customer protection is provided by Consumer Duty.

Question 16: Are there any equality and diversity issues that may arise from the proposals?

We cannot foresee any direct diversity and inclusion implications. The removal of affordability assessments or increased access to execution-only transactions, could potentially increase the risk of harm to borrowers focussed on short term benefits, those with lower financial literacy, vulnerable customers or ageing customers.

The potential for harm could be reflective of the individual's circumstances, and firms would need to consider controls to mitigate the risks to these customers.

Question 17: Do you agree that given the permissive nature of the proposed changes, if adopted, an implementation period would not be necessary?

Although the changes proposed are permissive, we are mindful that there is a discussion paper on the future of the mortgage market expected over the summer.

Our recommendation would be to not implement any changes until the closure of that paper and analysis of the responses. There is a risk of unintended consequences with incremental changes in isolation.

Question 18: Do you have any comments on the Cost Benefit Analysis in Annex 2?

We do feel that cost implications will impact firms differently depending on their size and system capabilities. Provided the changes remain permissive, whilst this may lead to inconsistencies in implementation among firms, from a cost perspective it does place cost-based decision and priorities in the firms' control.